

**REPORT OF THE AUDITOR-GENERAL TO THE NORTH WEST PROVINCIAL LEGISLATURE  
AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE  
INFORMATION OF THE CITY OF MATLOSANA FOR THE YEAR ENDED 30 JUNE 2009**

**REPORT ON THE FINANCIAL STATEMENTS**

**Introduction**

1. I was engaged to audit the accompanying financial statements of the City of Matlosana which comprise the statement of financial position as at 30 June 2009, statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes, as set out on pages [xx] to [xx].

**The accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the Statements of Generally Recognised Accounting Practice (GRAP) and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

**The Auditor-General's responsibility**

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the International Standards on Auditing and *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.
4. Paragraph 11 *et seq.* of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is not effective for this financial year, I have determined that my audit of any disclosures made by the City of Matlosana in this respect will be limited to reporting on non-compliance with this disclosure requirement.

**Basis for disclaimer of opinion**

**Property, plant and equipment**

5. As reported in the prior year, my opinion on property, plant and equipment of R534 358 454 was modified. During the year under review, management did not implement corrective measures on the qualification raised in this regard. As a result thereof, I was unable to verify the opening balances other than agreeing them to the prior year audited financial statements.
6. Capital expenditure of R120 647 267 have been capitalised to infrastructure assets prior to final project completion certificates being obtained. Infrastructure assets are therefore overstated and work in progress understated by R120 647 267.
7. I was unable to obtain sufficient appropriate audit evidence for the existence of infrastructure assets with a cost of R133 743 250 and accumulated depreciation of R82 426 790, as these assets could not be physically verified. Consequently I did not obtain all the information and audit evidence I considered necessary to establish the valuation and existence of infrastructure assets.

8. The municipality did not review the useful life of property, plant and equipment on an annual basis as required by the Statement of Generally Recognised Accounting Practice, GRAP 17 *Property, plant and equipment*. I was therefore unable to determine whether the impact of the change in estimate of the depreciation charge would be material to the financial statements.
9. I was unable to obtain sufficient appropriate audit evidence for land with a cost of R44 685 527 held in the municipality's name. The records of the municipality did not permit me to perform alternative audit procedures. I was therefore unable to verify the existence, rights and obligations, completeness and valuation of land and buildings disclosed in note 9 to the financial statements.

### **Long and short-term receivables**

10. Long-term receivables as disclosed in note 10 to the financial statements include the short-term portion of the long-term receivables for housing stands. The records of the municipality did not permit me to calculate the short-term portion as required by the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of financial statements*, consequently I was unable to determine the valuation of long-term receivables.
11. I was unable to obtain sufficient appropriate audit evidence for the Sale of housing stands balance of R1 694 939 and the Housing: houses balance of R9 951 623 disclosed in note 10 to the financial statements. The municipality also did not consider the recoverability of these balances as required by the South African Statement of Generally Accepted Accounting Practice, IAS 39 (AC 133) *Financial instruments: Recognition and measurement*, as evidenced by the fact that they were not included in the municipality's bad debt provision. I was therefore unable to verify the existence, completeness and valuation of these long-term receivables.

### **Consumer debtors**

12. As reported in the prior year, my opinion on the provision for bad debts was modified. During the year under review, management did not implement corrective measures in this regard. As a result thereof, I was unable to verify the opening balance other than agreeing it to the prior year audited financial statements.
13. The municipality's calculation of the provision for bad debts of R585 032 001 disclosed in note 12 to the financial statements could not be adequately substantiated by an approved council policy, nor is it in line with paragraphs 58 and 59 of the South African Statement of Generally Accepted Accounting Practice, IAS 39 (AC 133) *Financial instruments: Recognition and measurement*.

### **Other debtors**

14. As reported in the prior year, my opinion on other debtors of R100 616 620 was modified. During the year under review, management did not implement corrective measures on the modification raised in this regard. As a result thereof, I was unable to verify the opening balance other than agreeing them to the prior year audited financial statements.
15. I was unable to obtain sufficient appropriate audit evidence for other debtors of R142 227 177 and the provision for bad debts of R84 684 421 disclosed in note 13 to the financial statements. The municipality's records do not permit the performance of alternative procedures. I was therefore unable to verify the existence, rights and obligations, completeness and valuation of other debtors of R57 542 756 disclosed in the statement of financial position.

### **Long-term liabilities and infrastructure assets**

16. In the prior year my opinion on long-term liabilities and infrastructure assets were further modified regarding the altered functions and powers of the municipality determined by the Minister for Provincial and Local Government as per *Government Notice No. 821 of 2003*, issued in *Government Gazette No. 25076 of 13 June 2003*, whereas certain assets and liabilities on bulk water and sewerage services were to be transferred from the Dr. Kenneth Kaunda District Municipality to the City of Matlosana. As at the end of the financial year, these

long-term liabilities and infrastructure assets had not been transferred, resulting in long-term liabilities being understated by R30 026 199 and infrastructure assets being understated by an unknown amount due to inadequate information.

### **Provisions and liabilities**

17. As reported in the prior year, my opinion on the provision for leave pay of R8 884 528 was modified. During the year under review, management did not implement corrective measures on the modification raised in this regard. As a result thereof, I was unable to verify the opening balance other than agreeing it to the prior year audited financial statements.
18. Management did not raise a provision for the restoration of the landfill site near Orkney, in line with the requirements of the Statement of Generally Recognised Accounting Practice, GRAP19 *Provisions, contingent liabilities and contingent assets*. I was unable to determine the misstatement of the provision and the expenditure.

### **Creditors**

19. All creditors, trade and other, are paid at year-end based on invoices that have been received in the month of June. Outstanding cheque payments totalling R37 839 759 have not been reversed to trade creditors at year-end. Creditors and bank and cash balances disclosed in the statement of financial position are therefore understated by the said amount.

### **Unspent conditional grants and receipts**

20. I was unable to obtain an explanation for the difference of R9 842 906 in grants and subsidies received of R242 823 264 as per third party confirmation and the amount of R232 980 358 recognised as revenue in the statement of financial performance. I was unable to perform alternative procedures and consequently was unable to verify the completeness, accuracy and occurrence of revenue of R232 980 358 disclosed in the statement of financial performance and the valuation and completeness of unspent conditional grants and receipts of R49 204 429 disclosed in the statement of financial position.

### **Funds and reserves**

21. As reported in the prior year, my opinion on funds and reserves of R22 774 543 was modified. During the year under review, management did not implement corrective measures in this regard. As a result thereof, I was unable to verify the opening balance other than agreeing it to the prior year audited financial statements.
22. Contrary to the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of financial statements*, there are movements in reserves disclosed on the face of the statement of financial position. The only funds that should be disclosed are the housing fund and the accumulated surplus. The additional, prohibited movements shown are pension reserve, capital replacement reserve, self insurance reserve, government grant reserve, donations and public contribution reserve and capitalisation reserve. This disclosure deficiency is material to the financial statements.
23. The combined carrying value of property, plant and equipment of R125 715 977 financed by the capital replacement reserve, capitalisation reserve and the donations and public contributions reserve as per the asset register, differed with the combined balance of R38 014 685 of these reserves as disclosed in the statement of changes in net assets. The difference of R87 701 292 could not be substantiated. The municipality's accounting records did not permit alternative procedures to be performed. Consequently I am unable to verify the valuation and completeness of reserves amounting to R38 014 685.
24. There is no clear documented basis of the quantification of risk into monetary terms for the self-insurance reserve. I could not establish the rationale for the estimation of the reserve and was therefore unable to conclude on the sufficiency or accuracy of the balance of R12 224 735 as disclosed in the statement of financial position.

Given the above, I could not determine the completeness, valuation and allocation of funds and reserves disclosed in the statement of financial position.

### **Cash and bank**

25. As reported in the prior year, my opinion on the cash and bank balance was modified. During the year under review, management did not implement corrective measures on the modification raised in this regard. As a result thereof, I was unable to verify the opening balance other than agreeing it to the prior year audited financial statements.

### **Accumulated surplus**

26. As reported in the prior year, my opinion on various items of revenue totalling R229 076 408 and expenditure totalling R28 118 116 were modified. During the year under review, management did not implement corrective measures on the modification raised in this regard. As a result thereof, I was unable to verify the opening balance of accumulated surplus other than agreeing it to the prior year audited financial statements.

### **Financial instruments**

27. Financial Instruments disclosure as required by the South African Statement of Generally Accepted Accounting Practice, IFRS 7 *Financial instruments disclosure* and IAS 32 *Financial instruments presentation* has not been included in the financial statements. I am unable to quantify the impact of the non-disclosure so as to determine whether it is material to the financial statements. However given the materiality of the financial assets and liabilities, this non-disclosure may have a material impact on the financial statements as a whole.

### **Disclaimer of opinion**

28. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

### **Emphasis of matters**

I draw attention to the following matter on which I do not express a disclaimer of opinion:

### **Significant uncertainties**

29. During the year net withdrawals of R109 209 571 were made from call investment deposits for the purpose of funding operating expenditure. Due to the fact that these withdrawals were not budgeted for and the municipality did not have an appropriate cash management and investment policy as required by section 13(2) of the MFMA, I was unable to determine whether appropriate approvals for these withdrawals were obtained.

### **Unauthorised, irregular or fruitless and wasteful expenditure as well as material losses through criminal conduct**

30. As disclosed in note 28 to the financial statements, unauthorised expenditure of R34 995 and fruitless and wasteful expenditure of R4 056 958 incurred in the prior year has not yet been considered by council in terms of section 32 of the PFMA.

### **Other matters**

I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

### **Unaudited supplementary schedules**

31. The municipality provided supplementary information in the financial statements on whether resources were obtained and used in accordance with the legally adopted budget, in accordance with GRAP 1: *Presentation of financial statements*. The supplementary budget

information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. Accordingly I do not express an opinion thereon.

### **Non-compliance with applicable legislation**

#### 32. Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA)

- Contrary to section 62, no risk assessment was performed in the year under review.
- Contrary to section 63(2) (a), the fixed asset register was not properly maintained.
- Contrary to section 131(1), the municipality did not address the findings raised in the prior year audit report.

#### 33. Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA)

- Contrary to section 104, the municipality did not have a fraud prevention plan.

### **Governance framework**

#### 34. The governance principles that impact the auditor's opinion on the financial statements are related to the responsibilities and practices exercised by the accounting officer and executive management and are reflected in the internal control deficiencies and key governance responsibilities addressed below:

### **Internal control deficiencies**

#### 35. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the deficiencies in the system of internal control, which led to the disclaimer of opinion. The root causes are categorised according to the five components of an effective system of internal control. In some instances deficiencies exist in more than one internal control component.

<b>Par. no.</b>	<b>Basis for disclaimer of opinion</b>	<b>CE</b>	<b>RA</b>	<b>CA</b>	<b>IC</b>	<b>M</b>
5-9	Property, plant and equipment	5		3;4 ;5		
10-11	Long and short-term receivables	5		4		
12-13	Consumer debtors			5,6		
14-15	Other debtors	5		4		
16	Long-term liabilities and infrastructure assets	5		4		
17-18	Provisions and liabilities	5		4;6	1	
19	Creditors	5		3;4		
20	Unspent conditional grants and receipts	5		4		
21-24	Funds and reserves	5		4		
25	Cash and bank			4		
26	Accumulated surplus			4		
27	Financial instruments			4		1

<b>Legend</b>	
<b>CE = Control environment</b>	
The organisational structure does not address areas of responsibility and lines of reporting to support effective control over financial reporting.	1
Management and staff are not assigned appropriate levels of authority and responsibility to facilitate control over financial reporting.	2
Human resource policies do not facilitate effective recruitment and training, disciplining and supervision of personnel.	3
Integrity and ethical values have not been developed and are not understood to set the standard for financial reporting.	4
The accounting officer/accounting authority does not exercise oversight responsibility	5

over financial reporting and internal control.	
Management's philosophy and operating style do not promote effective control over financial reporting.	6
The entity does not have individuals competent in financial reporting and related matters.	7
<b>RA = Risk assessment</b>	
Management has not specified financial reporting objectives to enable the identification of risks to reliable financial reporting.	1
The entity does not identify risks to the achievement of financial reporting objectives.	2
The entity does not analyse the likelihood and impact of the risks identified.	3
The entity does not determine a risk strategy/action plan to manage identified risks.	4
The potential for material misstatement due to fraud is not considered.	5
<b>CA = Control activities</b>	
There is inadequate segregation of duties to prevent fraudulent data and asset misappropriation.	1
General information technology controls have not been designed to maintain the integrity of the information system and the security of the data.	2
Manual or automated controls are not designed to ensure that the transactions have occurred, are authorised, and are completely and accurately processed.	3
Actions are not taken to address risks to the achievement of financial reporting objectives.	4
Control activities are not selected and developed to mitigate risks over financial reporting.	5
Policies and procedures related to financial reporting are not established and communicated.	6
Realistic targets are not set for financial performance measures, which are in turn not linked to an effective reward system.	7
<b>IC = Information and communication</b>	
Pertinent information is not identified and captured in a form and time frame to support financial reporting.	1
Information required to implement internal control is not available to personnel to enable internal control responsibilities.	2
Communications do not enable and support the understanding and execution of internal control processes and responsibilities by personnel.	3
<b>M = Monitoring</b>	
Ongoing monitoring and supervision are not undertaken to enable an assessment of the effectiveness of internal control over financial reporting.	1
Neither reviews by internal audit or the audit committee nor self -assessments are evident.	2
Internal control deficiencies are not identified and communicated in a timely manner to allow for corrective action to be taken.	3

36. The municipality did not have a chief financial officer for the past financial year. The deputy financial manager was assisted by consultants to perform the financial reporting function. They were assisted by inexperienced staff from the municipality, resulting in the number of findings raised during the audit. Furthermore, policies, procedures and proper controls were not in place for the year under review, whilst actions to identify and address risks to achieve financial reporting objectives were not taken.

#### **Key governance responsibilities**

37. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of key governance responsibilities, which I have assessed as follows:

No.	Matter	Y	N
<b>Clear trail of supporting documentation that is easily available and provided in a timely manner</b>			
1.	No significant difficulties were experienced during the audit concerning delays or the availability of requested information.		N
<b>Quality of financial statements and related management information</b>			
2.	The financial statements were not subject to any material amendments resulting from the audit.		N
3.	The annual report was submitted for consideration prior to the tabling of the auditor's report.	Y	
<b>Timeliness of financial statements and management information</b>			
4.	The annual financial statements were submitted for auditing as per the legislated deadline in section 126 of the MFMA.	Y	
<b>Availability of key officials during audit</b>			
5.	Key officials were available throughout the audit process.		N
<b>Development and compliance with risk management, effective internal control and governance practices</b>			
6.	Audit committee		
	<ul style="list-style-type: none"> <li>• The municipality had an audit committee in operation throughout the financial year.</li> <li>• The audit committee operates in accordance with approved, written terms of reference.</li> <li>• The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.</li> </ul>	Y	
7.	Internal audit		
	<ul style="list-style-type: none"> <li>• The municipality had an internal audit function in operation throughout the financial year.</li> <li>• The internal audit function operates in terms of an approved internal audit plan.</li> <li>• The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.</li> </ul>	Y	
8.	There are no significant deficiencies in the design and implementation of internal control in respect of financial and risk management.		N
9.	There are no significant deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.		N
10.	The information systems were appropriate to facilitate the preparation of the financial statements.		N
11.	A risk assessment was conducted on a regular basis and a risk management strategy, which includes a fraud prevention plan, is documented and used as set out in section 62(1)(c)(i) of the MFMA.		N
12.	Delegations of responsibility are in place, as set out in section 79 of the MFMA.	Y	
<b>Follow-up of audit findings</b>			
13.	The prior year audit findings have been substantially addressed.		N
14.	PPAC/Oversight resolutions have been substantially implemented.		N/A
<b>Issues relating to the reporting of performance information</b>			
15.	The information systems were appropriate to facilitate the preparation of a performance report that is accurate and complete.	Y	
16.	Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.	Y	
17.	A strategic plan was prepared and approved for the financial year under review for purposes of monitoring the performance in relation to the budget and delivery by the City of Matlosana against its mandate, predetermined objectives, outputs, indicators and targets as per section 68 of the MFMA.	Y	

No.	Matter	Y	N
18.	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.	Y	

38. There was an overall lack of effective supervision, monitoring and leadership within the municipality, resulting in a poor governance environment.

#### **Late finalisation of the audit report**

39. In terms of section 126(3)(b) of the MFMA I am required to submit my report to the municipal manager within three months of the receipt of the financial statements. In the interest of improving accountability and due to the process implemented by me to ensure consistency in the manner in which material audit findings are reported, I have delayed the finalisation of my report to 30 April 2010.

### **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

#### **Report on performance information**

40. I have reviewed the performance information as set out on pages xx to xx.

#### **The accounting authority's responsibility for the performance information**

41. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality, prepared by the municipality in terms of section 46 of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

#### **The Auditor-General's responsibility**

42. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.

43. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.

44. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

#### **Findings on performance information**

#### **Existence and functioning of a performance audit committee**

45. The municipality did not appoint or budget for a performance audit committee, nor was another audit committee utilised as the performance audit committee, as required by regulation 14(2) of the Municipal Planning and Performance Management Regulations, 2001.

#### **Usefulness and reliability of reported performance information**

46. The following criteria were used to assess the usefulness and reliability of the information on the municipality's performance with respect to the objectives in its integrated development plan:

- Consistency: Has the municipality reported on its performance with regard to its objectives, indicators and targets in its approved integrated development plan.
- Relevance: Is the performance information as reflected in the indicators and targets clearly linked to the predetermined objectives and mandate. Is this specific and measurable, and is the time period or deadline for delivery specified.
- Reliability: Can the reported performance information be traced back to the source data or documentation and is the reported performance information accurate and complete in relation to the source data or documentation.

The following audit findings relate to the above criteria:

#### **Reported performance information not relevant**

47. The following key performance indicators and quarterly projected targets with regard to the Directorate: Corporate governance/good governance and public participation were not:

- specific in clearly identifying the nature and the required level of performance
- measurable in identifying the required performance

Objectives	Key Performance Indicators	Quarterly Projected Target	Target Date
To effectively protect Council's interest	No of policies received by June 2009	Nr of policies Nr of policies	Jun 09
	No of research notes compiled by June 2009	Nr of notes Nr of notes	
	No of informal advice given by June 2009	Nr of advice Nr of advice	
To ensure institutional capacity to implement programmes established and a conducive environment for shared growth created	Sustainable community investment programmes introduced and implemented by June 2009	No of programmes	Jun 09
		No of programmes	
		No of programmes	
		No of programmes	
To ensure institutional capacity to implement programmes established and a conducive environment for shared growth created	Total rand value of contracts awarded by June 2009	R value awarded	Jun 09
		R value awarded	
		R value awarded	
		R value awarded	

#### **APPRECIATION**

48. The assistance rendered by the staff of the City of Matlosana during the audit is sincerely appreciated.

Pretoria

Date of signing



AUDITOR - GENERAL  
SOUTH AFRICA

Auditing to build public confidence